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SUBJECT: SERBIA: WEDDED TO COAL FOR ENERGY AND POLITICAL NEEDS

REF: 09 BELGRADE 1482

SUMMARY

11. (SBU) Serbia remains deeply wedded to coal to fuel its energy needs. Despite ongoing efforts to further diversify energy resources to include more hydropower and renewable energy (Ref A), Serbia's natural abundance of coal has assured that the fossil fuel will have a primary place in meeting Serbia's - and the region's - energy needs for the coming fifty years. In order to provide supply and meet demand, Serbia's coal industry is hoping for nearly \$1 billion in investments over the next ten years, providing commercial opportunities for western firms. In addition to its economic significance, Serbia's coal industry and its militant miners remain a political force, which has proven in the past its ability to topple governments and to fund political parties. This dirty fuel remains a dirty but lucrative business in Serbia. End Summary.

KOLUBARA MINE

12. (U) The Kolubara open pit coal mine, located 40 miles southwest of Belgrade in the municipality of Lazarevac, is Serbia's largest coal producer, responsible for 70% of the country's lignite. Kolubara produces 30 million tons annually and has 2.2 billion tons of reserves. (By comparison, Kosovo's fields produce 7.1 million tons per year and have 12 billion tons of reserves.) Kolubara is owned by Serbia's state owned electric power industry, EPS, and nearly 90% of Kolubara's coal is used for electricity production at EPS' four thermo-power plants. The rest of Kolubara's coal is used either for domestic heating or is exported, primarily to Romania.

ENOUGH COAL TO LAST UNTIL 2060

13. (U) Kolubara currently has four fields in operation and intends to open two new fields to replace the current ones over the next several years, Kolubara's Deputy Director Vladan Radovanovic told us during a December 21 visit to the mine. Kolubara's two oldest lignite fields opened in 1955 and 1961 and currently have 10 to 40

million tons of reserves left, which could continue producing for the next six to eight years. The newest lignite field opened in 1994, and is scheduled to operate until 2045 with annual production averaging 12 million tons. Radovanovic said that starting in 2010 Kolubara would prepare to open two new fields to replace the oldest ones. For those new fields Kolubara would need equipment including excavators and conveyor systems valued at more than \$700 million. Currently, Kolubara uses primarily German equipment. Radovanovic said the German Government had shown great interest in providing grants and soft loans to Kolubara since October 2000. These new lignite fields should satisfy Serbia's needs for coal until 2060, Radovanovic said.

FROM COAL TO ELECTRICITY: NIKOLA TESLA THERMO POWER PLANTS

¶4. (U) With 3,288 MW of installed capacity at its four thermoelectric power plants, EPS' daughter company TPP Nikola Tesla provides 36% of Serbia's total electricity capacity and is the largest producer of electricity in South-East Europe. Combined, the four thermal power plants (TENT A, TENT B, Kolubara A and Morava) provide 18 billion kWh annually, around 47% of EPS' total production. Together, these four plants consume 27 million tons of Kolubara's coal annually, with TENT B alone consuming 60,000-80,000 tons of lignite per day. To feed this constant demand, TPP Nikola

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Tesla operates its own railway system taking the coal directly from Kolubara to the power plants. The EPS coal train is the only railway system permitted to operate independently of the state-owned Serbian Railways in Serbia.

¶5. (SBU) Aleksandar Vlajcic, Assistant Manager at TPP Nikola Tesla, told us during a December 21 visit to the facility that Serbia and the region is dependent upon the coal powered plants and the coal fields that feed them. As an example, he cited the January 2009 power shortages in Europe when Russia cut off natural gas supplies to Ukraine. Vlajcic said during those weeks the power plants and mines operated at full capacity to maintain Serbia's and the region's electricity supply and to avoid spikes. He said Serbia was essential for the functioning of the regional electricity grid, since Serbia bordered and was connected to the electricity grids of its eight neighbors (including Kosovo). He proudly noted that without Serbian electricity the EU grid would not function since Serbia connected the EU's southern members (Bulgaria and Greece) with its western and northern members.

KOLUBARA'S POLITICAL INFLUENCE IN SERBIA

¶5. (SBU) In addition to its economic significance, the coal industry and its militant miners remains a significant political force in Serbia, requiring the constant courting and caution of political leaders. Currently, Kolubara employs 10,500 people out of 30,200 in EPS in Serbia proper. (Counting workers still on its payroll in Kosovo, EPS has 35,800 employees.) Although it has cut back from having 17,000 workers in 2000, Kolubara still employs more workers than Telekom Srbija (9,500) and has a similar number of employees as Serbia's NIS petroleum industry (11,000).

¶6. (SBU) The 17,000 employees of Kolubara played a key role in bringing down the regime of late Slobodan Milosevic in October 2000

when they halted coal production in protest of Milosevic's election fraud and refusal to step down. Despite threats from the army and EPS, the miners showed their support for democratic presidential candidate Vojislav Kostunica. The halt in coal production further weakened Milosevic, who was toppled just days later. One year later, the miners' demand for higher salaries challenged the still-fragile democratic government. The threat of a strike forced then-PM Zoran Djindjic to come personally to Kolubara for direct negotiations with the miners to resolve the problem and to save his government.

DIRTY MONEY FROM A DIRTY BUSINESS

¶17. (SBU) As they do with other state-owned companies in Serbia, ruling political parties use Kolubara and its resources for personal and party interests. Aleksandar Kovacevic, an independent energy economist for the UNDP, told us in June 2009 that when Kostunica's Democratic Party of Serbia (DSS) controlled the mines in 2008 party bosses serving as mine managers would illegally sell coal to fill both their personal and party coffers. Party officials working at Kolubara also found creative ways to profit from the mine's enlargement plans, according to Kovacevic; as Kolubara spent millions of dollars per year to buy surrounding property, party bosses would sell "movable houses" to the company multiple times.

¶18. (SBU) The DSS lost control of both EPS and Kolubara when Boris Tadic's Democratic Party (DS) and the Socialist Party of Serbia (SPS) formed the new national government in July 2008. In July 2009, the DS- led government appointed Nebojsa Ceran as Kolubara's director, replacing former DSS director Dragan Tomic. (Ceran also serves as a DS Member of Parliament.) Some daughter companies spun off from Kolubara in 2005 are currently controlled by the SPS because the local government in Lazarevac (the municipality where

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the mine is located) is comprised of a DSS-NS-Serbian Radical Party and SPS coalition.

¶19. (SBU) In September 2009, Belgrade mayor and DS Vice President Dragan Djilas accused former Director Tomic of spending more than \$150 million over five years on renting transport and equipment from private individuals and companies. Soon after, Serbia's tax police submitted criminal charges for tax evasion against Tomic. Goran Perisic, Chief of Staff in Kolubara, told us on January 5 that he suspected the accusations were a politically-motivated DS effort to further weaken the DSS.

¶10. (SBU) After becoming director, Ceran announced efforts to cut costs and to introduce public tenders for Kolubara projects. The impact of these changes has yet to be seen, however. In 2009 Kolubara spent \$15 million to purchase expropriated land surrounding the mine. Kolubara Deputy Director Radovanovic told us that an additional \$3 million has been set aside in the budget to buy more land. While currently there are no accusations of corruption against the DS management, the amount of funds required for purchasing equipment and land leaves open significant opportunities for internal malfeasance. The government, the parties and EPS will need to continue to reform if they are to significantly reign in corruption in the sector.

COMMENT

¶11. (SBU) While Serbia plans to diversify its energy resources, coal will remain the primary fuel for the next few decades thanks to its natural abundance and the potential it presents for political patronage and graft. Ultimately, Serbia's efforts to clean up its air will be directly tied to its ability to clean up the power and influence of the politically-charged domestic coal industry. End Comment.

BRUSH